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No. 92-1142

IN THE
Supreme Court of the United States
OCTOBER TERM, 1992

CHARTER FEDERAL SAVINGS BANK,
Petitioner,

v.

DIRECTOR, OFFICE OF THRIFT SUPERVISION, *et al.*,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Fourth Circuit

REPLY MEMORANDUM TO BRIEF FOR THE RESPONDENTS IN OPPOSITION

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The government has never disputed that it was the Federal Home Loan Bank Board ("FHLBB") that initiated the mergers in question, that it sought out Charter and requested that Charter merge with four troubled institutions that would otherwise have been seized and liquidated by federal regulators.[1] Petition at 4a, 6a, 7a.

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[1] The government implies that Charter itself was a troubled institution. *See* Resp. Br. at 2 (emphasis supplied) (noting that Charter agreed to merge with "*other* troubled Virginia savings institutions."). The implication is wrong, and is not supported anywhere in the record.

In fact, Charter intially declined to merge because assumption of the liabilities of the troubled thrifts would have rendered Charter insolvent and subject to an immediate government takeover. Petition at 5a. It was only after Charter negotiated specific assurances from the FHLBB that it could use the purchase method of accounting and treat the acquired institutions' deficit net worth as an intangible asset that Charter finally agreed to merge with the failing thrifts. Petition at 5a, 6a-7a.[2]

As a result of the mergers and in reliance on the terms of its agreement with the government, Charter assumed $62 million more in liabilities than in assets, and relieved the government of what would otherwise have been an expensive bailout of four savings and loans. Having reaped the windfall of Charter's acquisitions, *i.e.*, Charter has eliminated the majority of the deficit net worth it inherited, the government has instructed Charter that it can no longer treat the unamortized supervisory goodwill as a regulatory capital asset, leaving the 73 year old institution in noncompliance with the capital requirements and subject to seizure the moment the court of appeals' mandate is issued. The question before this Court is whether the government may repudiate its contractual obligations to Charter without according Charter a remedy.

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[2] The government quotes certain congressmen who characterize the purchase method of accounting as an "accounting gimmick" and as a "poison[]" of the industry. Resp. Br. at 3, 4 n.3. But it was the offer of supervisory goodwill that induced Charter to acquire four failing thrifts and to assume their substantial liabilities. As a result, the government was freed from the obligation to seize and liquidate these thrifts, and to pay tens of millions of dollars to the insured depositors. All the while, Charter has been in the process of eliminating the $62 million deficit net worth it inherited. In this context, it is apparent that the offer and use of supervisory goodwill, far from causing any losses, has inured to the benefit of the government and to the insurance fund. In any event, it was the government, not Charter, that created the concept and offered the use of goodwill as an asset to lure healthy savings associations to merge with their weaker sister institutions.

ARGUMENT

1. Charter seeks certiorari, in part, to resolve a conflict between the Fourth Circuit's decision in the instant case and the Ninth Circuit's decision in *Alpine Ridge Group v. Kemp*, 955 F.2d 1382 (9th Cir. 1992), *cert. granted*, 113 S. Ct. 490 (U.S. Nov. 16, 1992) (No. 92-551) (argument set for March 30, 1993). Petition at 9-10. Both cases pertain to the scope of the government's power to repudiate its contractual obligations, and address whether the government may exercise this power with impunity. Because this Court granted certiorari in *Alpine Ridge* and is hearing argument later this month, Charter requested that, if this Court is not inclined to grant Charter's petition at this time, the Court defer consideration of the petition until resolution of *Alpine Ridge*.

The government, in response, attempts to diminish the significance of *Alpine Ridge* and the conflict between the two circuits. Its attempts, however, are disingenuous and unavailing. For example, the government inexplicably relies on the Fourth Circuit's finding that Charter never secured an express promise that its right to treat supervisory goodwill as a regulatory capital asset would survive statutory changes, as if this fact distinguishes the case from *Alpine Ridge*. Resp. Br. at 12-13. To the contrary, Alpine Ridge likewise did not secure an express promise that the terms of its agreement would remain intact in the face of contrary legislation. But where the Fourth Circuit determined that the contract's silence regarding the effect of future legislation was fatal to Charter's claim, the Ninth Circuit found that the plaintiffs were entitled to a remedy.

The government further suggests that *Alpine Ridge* is irrelevant because the issues therein revolve around a different statute and a different contract. Resp. Br. at 12. However, the Ninth Circuit plainly held as a matter of law that *Bowen v. Public Agencies Opposed to Social Se-*

curity Entrapment, 477 U.S. 41 (1986), does not preclude *non-injunctive* relief to *any* plaintiff whose contract with the government has been frustrated by subsequent legislation. In direct conflict with *Alpine Ridge*, the Fourth Circuit, purportedly relying on *Bowen*, created "an additional, special rule of contract construction" applicable whenever the government is a party to an agreement. Petition at 18a. According to this "special rule," Congress can repudiate contracts to which the sovereign is a party without according a remedy to the aggrieved party. The Fourth Circuit's "special rule" transcends the facts in *Charter*, applies to every contract to which the government is a party, and is simply irreconcilable with the Ninth Circuit's holding. Given the broad implications of this conflict, review of the Fourth Circuit's decision is especially appropriate.

While the government states that "[t]his case need not be held" pending resolution of *Alpine Ridge*, Resp. Br. at 12, it never even intimates that such a brief delay would prejudice the public interest. In light of Charter's strong earnings, *e.g.*, Charter increased its tangible net worth in excess of $10 million last year alone,[3] it is difficult to discern, and the government fails to explain, how the public could be ill-served by deferring consideration of the petition until after *Alpine Ridge* is decided.

2. Arguing that this Court "does not ordinarily grant review to resolve a conflict between a court of appeals' decision and one or more trial court decisions," Resp. Br. at 12, the government dismisses out of hand two district court decisions[4] and three decisions from the federal court

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[3] *See* Affidavit of E.L. Byington, Jr. at ¶ 3 (Nov. 2, 1992) (attached to Charter's Motion to Stay Mandate filed in Court of Appeals on Nov. 2, 1992).

[4] *See Far West Federal Bank, S.B. v. Director, Office of Thrift Supervision*, 787 F. Supp. 952 (D. Or. 1992); *Security Federal Savings and Loan Association of Albuquerque v. Federal Savings and Loan Insurance Corporation*, 796 F. Supp. 1435 (D.N.M. 1991). The

with the most experience deciding contract cases against the government, the Court of Federal Claims.[5] Each of these cases applied *Bowen* in the manner urged by Charter here. These decisions, and the analyses therein, therefore strongly support Charter's conclusion that the Ninth Circuit's application of *Bowen* is correct, that the Fourth Circuit's application of *Bowen* is incorrect, and that the question on appeal is of significant national interest. Moreover, if one or more of these cases is affirmed on appeal, the respective plaintiff or plaintiffs would be entitled to substantial damages, a result greatly at odds with the almost certain seizure of Charter absent review by this Court.

3. While the government applauds the court of appeals' holding and stands by the court of appeals' reliance on *Bowen*, the government never addresses the context in which *Bowen* was decided or the stark differences between *Bowen* and the instant case, even though these differences were raised in Charter's petition.

First, *Bowen* involved a party's challenge of Congress' power to amend a statute. Charter, in contrast, does not contest Congress' authority to pass FIRREA and abrogate contracts. Rather, Charter submits, as the Ninth Circuit has found, that Congress' power to repudiate its own contractual obligations does not permit it to do so with impunity. *See Alpine Ridge*, 955 F.2d at 1385 (citation omitted) ("Here, the owners do not challenge Congress's power to amend the terms of the underlying

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government notes that another district court case, *Ensign Financial Corporation v. Federal Deposit Insurance Corporation*, 785 F. Supp. 391 (S.D.N.Y. 1992), dismissed the rescission count on reconsideration. *See Ensign*, No. 90 Civ. 5692, slip op. (Feb. 16, 1993). Even on reconsideration, however, the district court expressly rejected the government's interpretation of *Bowen*, *see id.* n.2, instead reversing on other grounds.

[5] *See Statesman Sav. Holding Corp. v. United States*, 26 Cl. Ct. 904 (Cl. Ct. 1992); *Winstar Corp. v. United States*, 25 Cl. Ct. 541 (1992); *Winstar Corp. v. United States*, 21 Cl. Ct. 112 (1990).

legislation in the exercise of 'public and general acts of a sovereign'.").

Second, this Court expressly found in *Bowen* that the term of its alleged contract revoked by Congress was *not*:

> a term over which the State had any bargaining power or for which the State provided independent consideration.

Bowen, 477 U.S. at 55. The agreement in *Bowen*, therefore, did not rise to a property interest protected by the Fifth Amendment. The contract here, in contrast, involves a bargained-for contractual right paid for with valuable consideration. *See also Alpine Ridge*, 955 F.2d at 1385 ("[The owners] assert that their contract rights are supported by independent consideration and are therefore vested under the Supreme Court's decisions in *Lynch* . . . and *Perry* . . . ."); *Acacia Villa v. Kemp*, 774 F. Supp. 1240, 1248 (C.D.Cal. 1990) ("[*Alpine Ridge*] falls into the category of cases that the *Bowen* Court was careful to distinguish. . . . The [respondents'] contracts are not gratuities; rather, they are bargained-for agreements, for which [respondents] paid valuable consideration. . . .").

Third, an analysis of the structure of the *Bowen* decision further undermines the Fourth Circuit's application of this Court's holding. The *Bowen* language relied upon by the Fourth Circuit is found in Part A of this Court's opinion. On its face, that language merely stands for the proposition that contracts cannot preclude Congress from passing corrective legislation unless the sovereign has unmistakably waived its right to do so. The Fourth Circuit, however, went beyond *Bowen*, concluding that Part A of *Bowen* also stands for the proposition that the government is relieved from any obligation to remedy its breach. Consistent with its misreading of *Bowen*, the Fourth Circuit found no need to address the issue of remedy:

> Given our holding, we need not rule on the appropriateness of rescission as a remedy.

Petition at 21a.

This Court, however, in Part C of the *Bowen* opinion, directly addressed the remedy question, concluding that no remedy was required because the right at issue did not arise from a contract. In sum, the court of appeals below found that it need not address Charter's right to a remedy even though this Court plainly found that the sovereign's right to pass legislation repudiating contracts does not, in and of itself, relieve the government of its obligation to remedy the breach.[6]

4. The government claims that the decision below is "firmly supported" by *Guaranty Fin. Serv., Inc. v. Ryan*, 928 F.2d 994 (11th Cir. 1991), and *Transohio Sav. Bank v. Director, Office of Thrift Supervision*, 967 F.2d 598 (D.C. Cir. 1992). Resp. Br. at 11. Consistent with Charter's reading of *Bowen*, however, both of these decisions applied the *Bowen* doctrine to cases in which the plaintiff sought *injunctive* relief that would tie Congress' hands and preclude it from breaching certain contracts. These cases, then, reaffirm the Ninth Circuit's interpretation of *Bowen*, and highlight the very distinction Charter has discussed above. *Indeed, the Fourth Circuit is the first court to apply the* Bowen *doctrine in a manner that precludes a plaintiff from obtaining relief other than injunctive relief. Neither this Court nor any other court of appeals has interpreted* Bowen *so broadly.*

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[6] The government not only failed to respond to differences between *Bowen* and the facts here, but it likewise failed to address Charter's concern that the court of appeals' interpretation of *Bowen* would render all government contracts illusory and unenforceable. *See* Petition at 17-18; *see also Murray v. Charleston*, 96 U.S. 432, 445 (1877) ("A promise to pay, with a reserved right to deny or change the effect of the promise, is an absurdity.").

5. The government relies on the court of appeals' gratuitous "findings" that "the FHLBB would not have intended to promise Charter continued treatment of supervisory goodwill as capital for the life of the amortization period," and that "it [is] doubtful . . . that the FHLBB intended to secure to Charter the use of supervisory goodwill over a fifteen to twenty-five year period." Petition at 20a-21a. Because "the interpretation of contractual language to discern contractual intent is a question of fact," *Painewebber Inc. v. Hartmann*, 921 F.2d 507, 510 (3d Cir. 1990),[7] and since there has never been an evidentiary hearing in the case, the Fourth Circuit's decision to rely upon what it believes were the government's intentions was error. The court of appeals' factual determinations are all the more inappropriate given the deposition testimony of Thurman Connell, the former Senior Vice President of the Federal Home Loan Bank of Atlanta.[8]

6. Finally, the government inexplicably includes in its opposition to Charter's petition two "additional grounds that independently support the court of appeals' judgment," even though the government acknowledges that the court of appeals did not address these issues, and that these questions are not ripe for this Court's consideration. Resp. Br. at 14. These issues were heavily briefed below, and in light of the current posture of these questions,

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[7] *See also Dawson v. General Motors Corp.*, 977 F.2d 369, 373 (7th Cir. 1992); *Jhaver v. Zapata Off-Shore Co.*, 903 F.2d 381, 384 & n.6 (5th Cir. 1990) (and cases cited therein).

[8] Mr. Connell testified that Charter and the government entered into "an agreement," that "the Bank Board had accepted it and they were willing to be bound by the terms that they had agreed to." Petition at 4-5. The court of appeals' "findings of fact" also ignored the context of the deal, that the Federal Savings and Loan Insurance Corporation was in desperate financial condition, that Charter's agreement to merge with the four troubled thrifts saved the government tens of millions of dollars, and that the extended amortization period was "the engine that made th[ese] transaction[s] go." Petition at 3-5.

Charter will not rehash the arguments here.[9] If this Court determines that the court of appeals erred in holding that *Bowen* relieves the government from according a remedy for Congress' repudiation of government contractual commitments, the court of appeals will have its opportunity on remand to address the issues raised but not addressed on appeal.

Respectfully submitted,

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[9] Suffice it to say that, while the government contends that the district court's order was an injunction in excess of the district court's statutory authority, the disrict court's order was actually a declaratory judgment. *See* Petition at 35a-36a ("This judgment is not restraining the government from acting or compelling it to act or expending public funds. It merely states the legal effect of actions it may take."). Even if the order could somehow be distorted into an injunction, neither 12 U.S.C. § 1464(d)(2) nor 12 U.S.C. § 1818(i) precludes injunctive relief *prior* to the appointment of a conservator or receiver. *See* Petition at 42a-45a. Moreover, resolution of the government's other argument, *i.e.*, that it would be impractical to effect rescission, would necessitate an evidentiary hearing.